Office Supreme Court, U. S.
FILED
OCT 16 1928
CHARLES ELMORE CROPLEY
CLERK

IN THE

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1928.

No. 46

THE UNITED STATES, PETITIONER,

v.

THE CAMBRIDGE LOAN AND BUILDING COMPANY.

ON WRIT OF CERTIORARI TO THE COURT OF CLAIMS.

BRIEF FOR RESPONDENT.

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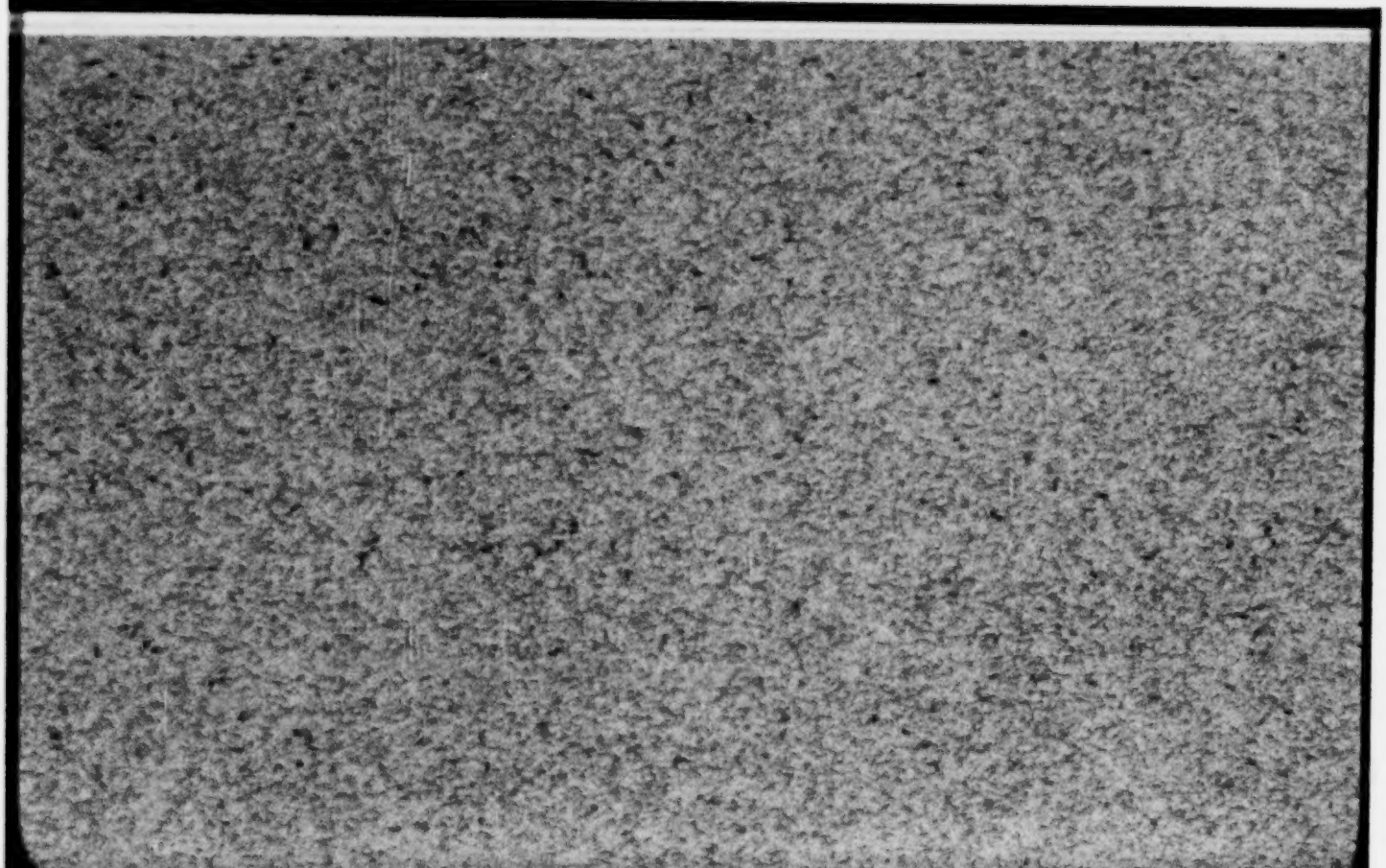

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ON WRIT OF CERTIORARI TO THE COURT OF CLAIMS.

BRIEF FOR RESPONDENT.

This case presents for determination three distinct major questions of law, namely:

1. Is the respondent exempt from income and profits taxes under the Revenue Act of 1918 for the calendar years 1918 to 1921, inclusive, as a "domestic building and loan association"?

2. Is the respondent exempt from income taxes under the Revenue Act of 1921 for the calendar years 1922 and 1923 as a "domestic building and loan association substantially all of whose business was confined to making loans to its members"?

3. Is the status of the respondent for the calendar year 1921 in respect of exemption controlled by the Revenue Act of 1918 or the Revenue Act of 1921?

The Court of Claims has held that respondent is exempt under the 1918 Act as a domestic building and loan association; that it is exempt under the 1921 Act as such an association which confined its business substantially to making loans to its members, and that for the calendar year 1921, up to November, 1923, of that year, its status is controlled by the Revenue Act of 1918 and for the remainder of the year by the Revenue Act of 1921.

Since we are dealing with statutes we shall approach the questions in the light of the rules laid down by this Court for their interpretation.

While there were similar statutes dealing with the exemption of building and loan associations enacted in 1866, 1894, and 1898, the present series of tax measures which has been uninterruptedly in effect for the past nineteen years had their origin with the enactment of the Act of August 5, 1909 (36 Stat. 112). This was followed by the Act of October 3, 1913 (38 Stat. 192), which remained in effect until September 8, 1916, when the Revenue Act of 1916 was enacted (39 Stat. 756). The 1916 Act remained in effect until Feb-

ruary 24, 1919, when the Revenue Act of 1918 was enacted (40 Stat. 1057). The 1918 Act, one of the statutes herein involved, remained in effect until November 23, 1921, when the Revenue Act of 1921, also involved herein, was enacted (42 Stat. 227).

The following are the provision for exemption of these associations contained respectively in these several acts:

The 1909 Act.

This Act provided at Section 38 that nothing therein contained shall apply to

> "Domestic building and loan associations *organized and operated exclusively for the mutual benefit of their members.*" (Italic letters supplied.)

The 1913 Act

This Act provided, at Paragraph (G) of Section II, that nothing therein should apply to

> "* * * Domestic building and loan associations. * * *"

The 1916 Act.

This Act at Section 231 thereof provided:

> "That there shall not be taxed under this Title any income received by—
>
> "4th. Domestic building and loan associations *and co-operative banks without capital stock organized and operated for mutual purposes and without profit.*" (Italic letters supplied.)

The 1918 Act.

"SEC. 231. That the following organizations shall be exampe from taxation under this Title (Part. III, Corporations):

"(4) Domestic building and loan associations *and co-operative banks without capital stock organized and operated for mutual purposes and without profit.*" (Italic letters supplied.)

The 1921 Act.

"SEC. 21. The following organizations shall be exempt from taxation under this title—

"(4) Domestic building and loan associations substantially all the business of which is confined to making loans to members; and co-operative banks without capital stock organized and operated for mutual purposes and without profit."

And in Title I, Section 1, certain definitions, of which the following are pertinent:

"That when used in this Act, the term 'domestic' when applied to a corporation or partnership means created or organized in the United States"; and

"The term 'United States', when used in a geographic sense, includes only the States, the Territories of Alaska and Hawaii, and the District of Columbia"; and

"The term 'corporation' included associations, joint stock companies, and insurance companies."

This Court has remarked: "One page of history is worth a volume of logic."

It is therefore appropriate to review the history of the particular legislation relating to exemption of these associations, the judicial interpretation and executive construction of the immediately preceding Acts in *pari materia*, in order to ascertain the intention of the Congress when on February 24, 1919, it enacted the Revenue Act of 1918 which controls this case for the several years 1918 to 1921, after which it will be simple to ascertain the intention of Congress when on November 23, 1921, it enacted the Revenue Act of 1921, which controls this case for the years 1922 and 1923.

I

The 1918 Act.

History of the Legislation

Beginning with the 1909 Act, we find that it exempted from taxation domestic building and loan associations *organized and operated exclusively for the mutual benefit of their members*.

Under this Act the Commissioner of Internal Revenue undertook to, and did, assess and collect taxes from these associations, resulting in the institution of several suits by the associations to recover the taxes paid (Parkview Building & Loan Association *v.* Herold, 203 Fed. 876, affirmed in Herold *v.* Parkview Building & Loan Association, 210 Fed. 577; Bellefontaine Building & Loan Co. *v.* McMaken, and Central Building, Loan & Savings Co. *v.* Bowland, 216 Fed. 526).

In the first of these cases, Parkview Building & Loan Association *v.* Herold, *supra*, the principal question was whether under the plan of operation of the association any inequality in the returns of the prepaying shareholder and the other shareholder in favor of the one or the other destroyed the mutuality among the shareholders required under the 1969 Act. The court held that it did not, using the following language:

> "Mutual credits are not necessarily equal credits; mutual debts need not be equal in amount. That the issuance of prepaid shares does not destroy the mutuality among the members of a building and loan association is the opinion of Judge Endlich, whose work on Building and Loan Associations is deemed an authority, as may be seen in his discussion of the subject in paragraphs 461 to 464. That view is also taken by the Supreme Court of Pennsylvania in Folk *v.* State Capitol Savings & Loan Association, 214 Pa. 529, 63 Atl. 1013, where the Supreme Court affirms the lower court, which was presided over by Judge Endlich. The following quotation from Judge Endlich's opinion in that case is helpful. He says (214 Pa. 535, 63 Atl. 1016):
>
> "'That the allowance of a fixed dividend upon such paid up stock out of the profits of the corporate business is a reasonable incident to its issuance, just to both classes of shareholders, and not calculated to give either an undue advantage over the other; that, on the contrary, the practical effect of the concurrent issuance of both installment and full paid stock is likely

> to prove beneficial to both classes of shareholders; that no essential characteristic of the building association scheme can be regarded as forbidding, and no essential purpose of it as defeated by this device; that it is contrary to no accepted rule of policy applicable to or involved in the nature of building associations.' "

This case was decided March 12, 1913, before the passage of the Revenue Act of 1913 and the decision was affirmed by the Circuit Court of Appeals for the Third Circuit on January 23, 1914, in Herold *v.* Parkview Building & Loan Association, *supra*.

The last case arose in the State of Ohio, being Central Building Loan & Savings Co. *v.* Bowland, and Bellefontaine Building & Loan Co. *v.* McMaken, *supra*, wherein again the exemption provision of the 1909 Act was at issue. There *the principal questions now before this Court* were disposed of. These questions as stated by the court are:

> "The allegations in the respective petitions which raise the question to be decided are, as to the first named plaintiff, 'that plaintiff for the mutual benefit of all its members *receives deposits from, and loans money to persons who are not members*, said acts being duly authorized by the law of Ohio;' and, as to the second named plaintiff, 'that since its organization said plaintiff has by its constitution provided that it is organized for the purpose of *raising money to be loaned to its members and to others and for the purpose of receiving money on deposit from time to time to the extent necessary to meet the demand made on it by its members, depositors*

and others; that, since its organization, said plaintiff has by its by-laws provided for the carrying out of each of said purposes, and has, from time to time, received deposits upon which it paid to the depositors the amount of interest due thereon, in accordance with the rate and terms upon which the deposits were made; that notwithstanding the said provisions of its constitution and by-laws authorizing the same, it has not made any loans to others than its members; and by virtue of the laws of the state of Ohio the plaintiff is, and at all times has been, authorizd and empowered to make loans to persons who are not members and to receive deposits from persons who are not members and to pay interest on deposits made by such persons.' The plaintiffs claim exemption from the tax under the proviso in the act. The government denies exemption on the ground, as to the first named plaintiff, that '*the corporation makes loans to and receives deposits from other than members*, and that accordingly in addition to its mutual features it does a business akin to a general banking business;' and, as to the second named plaintiff, that it is a corporation 'organized for the purpose of raising money *to be loaned to members and others*, and *that it is qualified to receive deposits or borrow funds from others than members*,' 'and, therefore, the government claims that these associations cannot be considered as organized and operated for the 'exclusive benefit,' or 'exclusively for the mutual benefit,' of their respective members. The government admits that the plaintiffs are domestic building and loan associations having features of mutuality between their members."

That is exactly the case at bar, and it is important to note the conclusions reached on the two principal questions involved:

> "If the power to borrow and loan from and to others than members takes building associations having it out of the class entitled to exemption, then the building and loan associations of most of the states must pay the tax. Since Congress by using the adjective 'domestic' necessarily had in mind associations formed *under State laws*, and since almost all such institutions have such powers under those laws, it may be said with some degree of certainly that Congress did not intend to deny them the exemption they otherwise would have simply because they had power to loan to persons not members, or to borrow from them."

Speaking of the Government's contention that an association accepting deposits and making loans to nonmembers is thereby engaging in the banking business, the court said:

> "Under this definition every building association is a bank, since it receives deposits, and, indeed, lends money to its members and, in most of the states, to persons not members. But they are building associations nevertheless, whose profits inure exclusively to the members themselves, and whose power and practice of borrowing money from nonmembers and lending to the same are only incidental to the main purpose for which they are formed, and are beneficial to, and in furtherance of, that purpose.

> "A nonmember borrowing or lending receives no benefit from the building association as such, but only the same benefit which he would receive by dealing generally with his money in the market. So he in no sense participates in the association, or in its profits. This participation is the exclusive right of each of the members, and every member receives the same benefit accruing to every other member. By this method of acquiring additional income for the association, there is no disturbance of the mutuality of interest, which is the distinguishing feature of building associations; indeed, by indulging in it the essential principle to that end underlying building associations is maintained."

On the subject of the effect of issuing different classes of stock the same court had this to say:

> "And it was held that such practice did not defeat equality and mutuality among the members of the association. If, under such circumstances as these and the other cases heretofore cited on the effect of the issuing of different classes of stock upon mutuality among members of the association, that quality is not impaired, how can it be successfully claimed that the necessary mutuality is destroyed when money is borrowed or loaned from or to persons who in no event are interested in the profits or losses of the association, but to which sustain the relation only of creditor or debtor, as the case may be?"

After reviewing the laws of Ohio and pointing out in great detail the care taken by the legislature of that State to preserve the integrity of these associations

and to supervise and annually inspect their operations, the court concluded as follows:

> "The conclusion is that building associations under the laws of Ohio, notwithstanding their power to borrow money from or loan money to nonmembers, are 'organized and operated exclusively for the mutual benefit of their members,' come strictly within the proviso giving them exemption from the tax in question, cannot be required to pay it, and the plaintiffs are entitled to recover the amounts paid by them under protest."

So it is that the Ohio Federal court, interpreting the 1909 Act containing the *restrictive clause* not contained in the 1913 Act and subsequent acts, held that the acceptance of deposits from and loans to others than members unequivocally granted to building associations under the Ohio laws did not operate to deny them exemption as domestic building and loan associations *operated exclusively for the* mutual benefit of their members. No appeal was taken from the decision of the Federal court in this case and it was accepted by the Federal Government as the correct interpretation of the 1909 Act. *The 1913 Act.* When the 1913 Act was introduced in the House of Representatives the exact language of the 1909 Act was incorporated restricting exemption of these associations as before to those *organized and operated exclusively for the mutual benefit of their members.* (H. R. 3321, April 21, 1913; Sec. II(G)). On May 8, 1913, the day the bill was passed by the House, the restricting clause in-

dicated in italics was deliberately stricken out and thus passed by the Senate, so that the Act simply provided that nothing therein should apply to "domestic building and loan associations."

Thus the 1913 Act exempted these associations without condition, provided only that they be "domestic." This act was in effect until September 8, 1916, and at no time thereunder was any building and loan association in the United States required to pay income taxes. The Government never disputed their unconditional exemption, and there is no case on record bringing in question their unconditional right to exemption under this act. This was the situation when on September 8, 1916, Congress enacted the Revenue Act of 1916.

The 1916 Act. This legislation began with the introduction of H. R. 16763, 64th Congress, 1st session. In Section XI (*a*) this bill provided for the exemption of "domestic building and loan associations," which was a reenactment of the 1913 Act, under the circumstances and conditions which existed, as have been pointed out. Bear in mind that the House bill also provided for the exemption of a number of other kinds of corporations that had not been previously exempted. This is called to your attention merely to show the increasing liberality of legislation in this regard. In this manner the bill passed the House, the same language being used as had been used in the 1913 Act. When the bill reached the Senate, we find that the Senate proposed an amendment to the House bill, known as amendment number 65, whereby the Senate sought to exempt *another kind of corporation* which had not been exempted by the

House bill, and this additional corporation it proposed to exempt in the same section with building and loan associations. To this amendment the House disagreed and the Conference Committee was then called upon to consider it, and we quote from page 4 of the Conference Report, dated September 7, 1916, being report number 1200, the following language:

> "Amendment Numbered 65.—'That the House recede from its disagreement to the amendment of the Senate numbered 65, and agree to the same with an amendment as follows:
>
> "'In lieu of the matter inserted by said amendment, insert the following: "and cooperative banks without capital stock organized and operated for mutual purposes and without profit, and a semicolon;" and the Senate agreed to the same.'"

Since the House bill contained only the language in the exemption clause "domestic building and loan associations," it is plain that the additional language agreed by the Conference Committee as offered by the Senate has nothing to do with building and loan associations, for the language which was added to the House bill was "and cooperative banks without capital stock, etc."

But if any doubt be entertained as to the purpose and intention of Congress, we refer to page 29 of the Conference Report, which contains the statement of the managers, on the part of the House, concerning their agreement in conference with the Senate. There

we find the explanation of the managers of the House of their agreement with the Senate on Amendment No. 65. This is the language used:

> "The Senate amendment provides that the income of cooperative banks organized and operated for mutual purposes and without profit shall be exempted from the income tax provision. The House recedes from its disagreement to the Senate amendment with an amendment exempting cooperative banks without capital stock organized and operated for mutual purposes and without profit."

The 1916 Act was in effect until February 24, 1919, and at no time that it remained the law was any effort made to subject any building and loan association to income taxes nor is there a case on record where there was brought in question their unconditional right to exemption. Under this Act the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, issued on Jan. 2, 1918, Regulations 33 (Revised) wherein at Article 68, paragraph 313, it was provided:

> "Par. 313. Unconditional.—Among the corporations exempt from the tax, without condition are * * * domestic building and loan associations, * * *"

And at paragraph 314 it was provided:

> "In all cases wherein the exemption is without condition and the Collector is satisfied that the organization comes within the exemptive

class he will be authorized to eliminate it from his list and relieve it from the necessity of making returns.

And at paragraph 315 it was provided:

"Corporations exempt under the Act of September 8, 1916, are also exempt from the war income tax imposed by Title I of the Act of October 3, 1917."

And at Article 70 of the same Regulations it is provided:

Art. 70. Domestic Building and Loan Associations.—A domestic building and loan association entitled to exemption is one organized under and pursuant to the laws of the United States or under and pursuant to the laws of some State or Territory thereof, and which is actually carrying on for the benefit of its members a building and loan association business in accordance with the laws under which it is organized. The fact that such an association issues fully paid or prepaid shares, calling for a specified rate of interest or dividends, will not disqualify it for exemption. The exemption is without qualification other than that the association is a domestic building and loan association. If a corporation by any other name is carrying on an exclusive building-and-loan business, before it is entitled to exemption it will be encumbent upon it to show to the satisfaction

> of the commissioner of internal revenue that it is in fact a building and loan association.

It is obvious that building and loan associations no longer occupied the attention of the executive department as they were unconditionally exempted and their names taken off of the Collector's list of taxable corporations. It is interesting to note that while this 1916 Act was still in effect the Commissioner of Internal Revenue was requested to furnish a ruling to the Building and Loan Commissioner of the State of California in respect of the exemption of certain kinds of California associations which, under the law, were empowered to and did make loans to others than shareholders and members and in respect of other associations that issued permanent or guarantee stock. The ruling of the Commissioner of Internal Revenue in conformity with the request of the California Commissioner was dated January 30, 1918, and is printed in the Appendix hereto. We quote the sum and substance of the ruling:

> "In reply you are informed that Building and Loan Associations organized and operated in accordance with the laws of the State in which they are organized and do business are exempt from the provisions of the law referred to above. Therefore, if a Building and Loan Association in your State, which transacts business in accordance with the information contained in your letter, does so under the authority conferred upon it by the laws of the State of California, then that fact does not destroy its exemption under the provisions of the acts cited."

Something else occurred while the 1916 Act was in effect. The Congress, on February 26, 1917, enacted a special Act (Chap. 129 printed in full in the Appendix hereto) which directed the Secretary of the Treasury to pay to the several building and loan associations therein named (including this respondent) the sums set forth therein, the same to be a refund of taxes "illegally collected from said associations under the Excise Tax Act of August 5, 1909." This Act was to enable all associations from whom taxes had been exacted under the early 1909 Act where the statute of limitations had tolled against refund claims, to recover all such taxes. All other associations from whom such taxes had been collected had already received refunds as the result of the decisions of the Federal courts hereinbefore cited interpreting the 1909 Act.

The foregoing is the history of the legislation and of the judicial interpretation and executive construction thereof at the time the Congress undertook on February 24, 1919, to enact the Revenue Act of 1918 with which we are primarily concerned in the case at bar.

The 1918 Act was a re-enactment, without change of a word, of the 1916 and 1913 Acts in respect of the exemption of building and loan associations. What interpretation must be given the intention of Congress then when it re-enacted the prior statutes which had been judicially interpreted, and construed by the executive department, in only one way uninterruptedly for ten years?

The 1918 Act. Can it be possible in the light of the history of this legislation for anyone to doubt what Congress intended? Every rule relating to the interpretation of statutes sustains the contention of the respondent that when the 1918 Act was enacted the Congress intended it to mean the same thing that it meant when it enacted the 1913 and 1916 Acts.

The 1918 Act was in effect with all the force of the prior statutes and their interpretation behind it until November 23, 1921, when the 1921 Act was enacted. It is appropriate at this point to very briefly review some of the cardinal principles of statutory interpretation which have been laid down by this Court for the guidance of the executive departments as well as the citizens.

The Language of the Statute. In U. S. *v.* Goldenberg, 168 U. S., 95, 102, we are told:

> "The primary and general rule of statutory construction is that the intent of the lawmaker is to be found in the language that he has used. He is presumed to know the meaning of words and the rules of grammar. The courts have no function of legislation, and simply seek to ascertain the will of the legislator. It is true there are cases in which the letter of the statute is not deemed controlling, but the cases are few and exceptional and only arise when there are cogent reasons for believing that the letter does not fully and accurately disclose the intent. *No mere omission, no mere failure to provide for contingencies, which it may seem wise to have specifically provided for, justify any judicial addition to the language of the statute.*" (Italic letters supplied.)

In U. S. *v.* Temple, 105 U. S., 97, 99, this court said:

> "Our duty is to read the statute according to the nature and obvious merit of the language without resorting to subtle and forced construction for the purpose of either limiting or extending its operation."

Again in Thompson *v.* U. S., 246 U. S., 547, 551, we find:

> "The intention of Congress is to be sought for primarily in the language used and where this expresses an intention reasonably intelligible and plain, it must be accepted without modification, by resort to construction and conjecture." (See also Gould *v.* Gould, 245 U. S., 151, 153.)

History of Legislation. In Guarantee Trs. Trust & S. D. Co. *v.* Sellers, 123 U. S. 276, this Court stated that the interpretation of the statute is often to be sought from the surrounding circumstances and the preceding history.

In U. S. *v.* Union P. R. Co., 91 U. S. 72, which has been exhaustibly cited, the rule is laid down that in construing a statute the courts may recur to the history of the times when it was passed, in order to ascertain the reason for its passage, as well as the meaning of its provisions.

In Smith *v.* Townsend, 48 U. S. 490, we are told that where the language of a statute is in any manner ambiguous or the meaning doubtful, resort may be had to the surrounding circumstances, the history of the

times and the defect or mischief which the statute was intended to remedy.

In Platt *v.* Union P. R. Co., 99 U. S. 48, it was held that in construing a statute, aid may be derived from attention to the state of things as it appeared to the legislature when the statute was enacted.

In Texas & P. R. Co. *v.* Interstate Commerce Commission, 162 U. S. 197, it was held that in construing the terms of a statute courts must take notice of the history of legislation, and of different possible constructions, select and apply the one that best comports with the genius of our institutions, and therefore most likely to have been the construction intended by the law-making power.

Adding Language Not Contained in the Statute. In Hobbs *v.* McLean, 117 U. S. 567, it was held that where a provision is left out of a statute either by design or mistake of legislation the courts have no power to supply, for to do so would be to legislate and not to construe.

In Yturbide *v.* U. S., 22 How. 290, it was held that where the legislature makes plain provision without any exception, the courts can make none (see also Maxwell *v.* Moore, 22 How. 185, and Pirie *v.* Chicago Title & T. Co., 182 U. S. 438).

Contemporaneous Executive Construction. This court has held that contemporaneous construction of a statute by the executive departments should be given great consideration—certainly where it is a practical construction (see Bank of the United States *v.* Halstead, 10 Wheat. 51; Slidell *v.* Grand Jean, 111 U. S.

412; Schell *v.* Forsche, 138 U. S. 562; Prigg *v.* Pa. 16 Pet. 539; Wetmore *v.* U. S. 10 Pet. 647).

Previous Statutes in Pari Materia. In U. S. *v.* Saunders, 22 Wall. 492, it was held that it is proper in construing a statute to ascertain the intention of the legislature from the language used in connection with the previous legislation on the same subject.

In U. S. *v.* Farden, 99 U. S. 10, it was held that other acts on the same subject and the connection of the words in the Act in question may be reviewed to determine the true intent and meaning of a provision in an Act of Congress; and in Virtebo *v.* Friedlader, 120 U. S., 707, it has also been held that all former statutes on the same subject whether repealed or unrepealed may be considered in construing provisions that remain in force.

In Vane *v.* Newcombe, 130 U. S. 220, it was held that in cases of doubt or uncertainty, acts in *pari materia* may be referred to in order to discern the intent of the legislation in the use of particular terms.

Judicial Interpretation of Prior Acts in Pari Materia. This Court has held that the meaning of a particular statute should be determined in the light of prior statutes in *pari materia* that have been judicially interpreted and construed (U. S. *v.* Saunders, 22 Wall. 492; U. S. *v.* Farden, 99 U. S. 10; Crane *v.* Newcombe, 132 U. S. 220; U. S. *v.* Central P. R. Co., 118 U. S. 235; The Aurora *v.* U. S. 7 Cranch, 382).

In the light of the foregoing, it seems obvious what, as a rule of decision, must be deemed to have been the intention of Congress when it enacted the Revenue Act of 1918.

In these circumstances it is rather immaterial what the Commissioner of Internal Revenue thereafter may have attempted to do by regulation, for no such regulation could possibly change the intention of Congress at the time it enacted the 1918 Act, as we have clearly demonstrated. It is interesting, however, to note the provisions of Article 515 of his Regulations 45, quoted in full in the Appendix (page 25) to the Government's brief. These Regulations 45 so quoted were promulgated by the Commissioner and approved by the Secretary of the Treasury January 28, 1921, after the 1918 Act had been in force for about two years. There it is stated:

> "* * * Where a building and loan association has no other features which render it liable to income tax, it will ordinarily not be subject to tax merely because—
>
> "(1) It has paid-up shares which are (a) preferred as to earnings, and (b) have a definite rate of interest which may be higher than the rate of dividends paid on other stock, or
>
> "(2) Its balance sheets show that *it is lending considerable sums to nonmembers*, or
>
> "(3) It is a regular borrower of large sums of money which it uses for loans to members, the dues paid by members being entirely inadequate for the business transacted by it."

There we find as late as January, 1921, the Commissioner acquiesces in the practice, which the Government now deprecates, of lending considerable sums to nonmembers, and nowhere can it be found that he

objects to the acceptance of deposits. These regulations were enacted only ten months prior to the passage of the 1921 Act. Can it be said that there existed any executive construction of this statute which placed building and loan associations in this country on notice up to January, 1921, that the making of loans to non-members or acceptance of deposits from them would debar them from exemption? The Commissioner did not so rule, nor had any court in the United States so ruled in interpreting the exemption provision of the 1918 or any preceding statute in *pari materia*.

Most particular attention is now invited to the next regulations promulgated by the Commissioner of Internal Revenue under this same 1918 Act quoted in full in the Appendix to the Government's brief (pages 26 and 27). These subsequent regulations were promulgated and approved June 16, 1921, six months after the regulations which we have just discussed. There we find in sub-paragraph (2) that he objects to accepting deposits unless they be used only for the purpose of making loans to members, and in sub-paragraph (3), while he still sanctions the making of loans in considerable sums to nonmembers, he states that it may only be done "in times of small demand" (whatever that means), and he has no objection "in times of small demand" to the investment of the association's funds (in what manner he does not state), which would otherwise lie idle and unproductive. In the second paragraph of sub-paragraph (4) he further, for the first time, informs these associations that where the facts show that they are borrowing large sums

of money from nonmembers with no reference to the borrowing needs of members and are loaning these sums to nonmembers, the number of depositors being disproportionate to the number of members (whatever that means) and the amount loaned to nonmembers being disproportionate to the amount loaned to members, such association will be deemed to be taxable and will be granted exemption only upon a satisfactory showing to the Commissioner "that it is, in fact, a *bona fide* building and loan association within the meaning of *this article*."

What force as a criterion upon which to establish long standing executive construction of an Act of Congress is a regulation promulgated four months before the law ceased to be in effect and two and one half years after it was enacted, especially under the circumstances which have been herein related?

This brings us to the 1921 Act, but, before passing on, it may be well to refer to the eminent authority, Judge Eudlich, whose reasoning in his work on Building and Loan Associations is in true accord with the decisions of the Federal courts, *supra*, interpreting the stringent provisions of the 1869 Act. We find at Section 313 of this work, written in 1882, the following:

> "It is said in Pennsylvania, and in Ohio, and seems to be the understanding of the law in Indiana, in Kansas, and in Massachusetts, that a building association has the power of lending its money to members only, and not to strangers. *It must be admitted that there is nothing in the reason or constitution of building associations, in favor of the doctrine. On the contrary, al-*

though it undoubtedly was their design that eventually all the members should become borrowers, in practice there is always a large portion of them who content themselves with paying, and never think of drawing out. Thus, if none but members may receive loans, the funds of the society may go begging; it may be subjected to constant losses on account of their lying idle; and the very end aimed at by the association, the speedy and profitable winding-up, be delayed by a restraint as unreasonable as the license is harmless. Yet, in the absence of special statutory authority giving that license, the doctrine denying it to building associations must be held to be established by authority." (Italic letters supplied.)

Singular it is, the author refers to the fact that at the time of writing (1882) the State of Ohio and four other States did not permit non-member loans, but the author states that whether or not an association may do this *depends upon the State statute*. However, as early as 1908, the State of Ohio by legislative enactment specifically authorized these associations to accept deposits from and make loans to non-members, and it is still the law. (See Ohio statute in Appendix.) All modern authors writing on the subject are in accord with Judge Endlich.

What do the Ohio laws provide respecting loans and deposits?

"Sec. 9647. Such corporation shall have all the powers set forth in the following sections of this chapter.

"SEC. 9648. To receive money on deposits, and all persons, firm, corporations and courts, their agents, officers and appointees may make such deposits and stock deposits, but such corporation shall not pay interest thereon exceeding the legal rate. When such deposits or stock deposits are made to the joint account of two or more persons, whether adults or minors, with a joint order to the corporation that such deposits or any part thereof are to be payable on the order of any one or more of such joint depositors, and to continue to be so payable notwithstanding the death or incapacity of one or more of the persons making them, such account shall be payable to any one or more of such survivors or survivor or order notwithstanding such death or incapacity. No recovery shall be had against such corporation for amounts so paid and charged to such account.

"SEC. 9657. To make loans to members and others on such terms, conditions and securities as may be provided by the association."

And, so it is that the Commissioner of Internal Revenue in retrospectively assessing in the year 1924 taxes against respondent for the years prior to the passage of the 1921 Act, namely, for the years 1918 to 1921, pretends that the Congress did not intend to exempt these associations under the provisions of the 1909 Act or the 1913 Act, or the 1916 Act, or the 1918 Act; that the successive re-enactment of this exemption provision over a period of 12 years was not intended as an adoption of the previous executive construction and judicial interpretation of prior acts; that he is not in any

manner bound thereby, nor by his own regulations and rulings; and that what the Congress intended and meant all along was to exempt only such associations that confine their loans substantially to members, a provision contained in the subsequent Act of November 23, 1921. The 1921 Act contained no retrospective provision respecting this exemption. This Court in the case of Shwab *vs.* Doyle, 258 U. S., 529, dealing with the subject of retrospective interpretation of statutes said:

> "If Congress, however, had the purpose assigned by the Commissioner, it should have declared it; when it had that purpose, it did declare it."

And further:

> "It is to be remembered that we are dealing with a tax measure, and whatever doubts exist must be resolved against it."

And further:

> "It is the proclamation of both that a statute should not be given a retrospective operation, unless its words make that imperative and this cannot be said of the words of the Act of September 8, 1916."

And further, in respect of the question of whether the declaration in the subsequent act was intended to express the purpose of the prior act, the court said:

> "And we cannot accept the explanation that this was an elucidation of the Act of 1916, and

> not an addition to it as averred by defendant, but regards the Act of 1918 rather as a declaration of a new purpose; not the explanation of an old one." ~~Court of Claims opinion~~.

Clearly, the 1918 Act and its predecessors are dead issues and cannot be revived at this late date by an attempt of the Internal Revenue Commissioner to place an interpretation thereon directly contrary to the intention of Congress, which has repeatedly re-enacted this statute in the light of prior executive construction and judicial interpretation of prior statutes in *pari materia*.

II.

The 1921 Act.

Now, on November 23, 1921, Congress decided to continue exempting these associations as they existed, upon condition that thereafter they confine their loans substantially to their members. Thus, the 1921 Act exempts the same associations which had been exempted from tax under every prior income tax law, or such of them as, in the future, confine their business substantially to making loans to members. In all other particulars and in all other respects Congress adopted the interpretation of the previous acts. It did not see fit to place any further restrictions upon them, such as prohibiting them from accepting deposits or requiring borrowers to subscribe to stock to the full amount of their loans, or to direct how they shall operate or conduct their business, or to in any way inter-

fere with the common practice existing among the associations in the various States other than in respect of the persons to whom they may make loans. The interpretation, therefore, of the 1921 Act becomes rather simple and requires only a practical determination of the extent to which these associations, after the passage of the 1921 Act, may indulge in making loans to nonmembers if they would retain their exempt status.

The Court of Claims has held that respondent, subsequent to the passage of the 1921 Act, has substantially complied with its provisions. Has it committed gross error? Is its judgment unsound or its conclusions illogical?

There are only two years (1922 and 1923) involved herein which are controlled by the provisions of the 1921 Act.

Bearing in mind that this act was passed only five weeks before the year 1922, and that its numerous provisions are not at once broadcast among the people of the cities, towns, and hamlets of the country, let us see what the facts are as found by the court. During these two years 90% of its loans and 87% of the money loaned was to members (see years 1922-1923—Finding VIII, Rec. 10). The Government contends that too large an *amount of money* was loaned to nonmembers during these two years. The question involves material rather than arbitrary consideration, bearing in mind the circumstances and necessities of the association upon the advent of the new act. If it has not grossly or materially overstepped the bounds

of a reasonable interpretation of the statute, it should not be denied exemption.

The word "substantially," used in the 1921 Act in respect of the making of loans to members, has been defined in "Words and Phrases, 2d Series, Vol. 4, page 753," as follows:

> "'Substantially' means in substance; in the main; essential; by including the material or essential part. See Town of Checotah *vs.* Town of Eufala, 110 Pac., 1014, 1019; Vannest *vs.* Murphy, 112 N. W., 236, 238; 135 Iowa, 123. See also Electric Candy Machine Co. *vs.* Morris, 156 Fed., 972, 974; Eisfeld *vs.* Kenworth, 50 Iowa, 389, 390."

In the case of South Penn Oil Co. *vs.* Knox, 69 S. E., 1020, 1021; 68 W. Va., 362, there was involved an oil and gas lease, describing the premises as being all that certain tract of land situated in a certain district of the waters of a designated stream bounded "substantially" as follows, etc. The court held that the word "substantially" there was intended to mean "about" or "in the main," as designated, and not "wholly" or "completely."

The courts have had occasion to consider what is meant by the words "substantially all" as used in a taxing statute, namely, the Revenue Act of 1918 which provided that consolidated returns of income and invested capital should be filed by affiliated corporations; and it defined affiliation to be, *inter alia*, where one corporation owns or controls "substantially all" of the stock of another corporation. This par-

ticular provision of the 1918 Act was before the U. S. District Court for the Eastern District of Missouri in the case of *In re* Temtor Corn & Fruit Products Co., 299 Fed. 326. After due consideration of the various contentions of the Government and the taxpayer the court reached the following conclusion:

> "The Commissioner, then, had no power to say, as he has said by his regulation, that 'substantially all of the stock of the other' means '95 per cent of the voting stock'. It is a matter for the courts to construe and not a matter about which the Commissioner may promulgate a regulation binding upon the courts.
>
> "Here in this case all of the voting stock was held by the bankrupt, though there were some 3,000 other stockholders holding preferred stock, which had no vote until dividends were passed for a stated period. I readily appreciate that the control of one corporation over another is ordinarily had by reason of control of the voting stock therein, and not through control of the non-voting stock. It is also true that no one is to be taxed, unless there exists a statute which authorizes the imposition of the tax. Such a statute is, however, to be given a reasonable construction, when it in fact exists, with a view to carrying out its purpose and intent. Here the purpose of Congress was to forestall such manipulation of profits of one corporation, through control by reason of voting stock, as would prevent the government from ascertaining correctly, and from collecting the sums justly due it, from excess profit taxes, of the controlled and affiliated corporations."

In conclusion the court observes:

> "From what is said, it follows that the construction of the word 'substantially' is also a matter for the courts, however valuable as a rule of practice and administration it may be to have fixed by the Commissioner a merely arbitrary standard."

It should be noted that the Commissioner has never attempted in any regulation to say what was meant by the words "substantially all" in the exemption provisions of the 1921 Act with which we are dealing.

The case just cited was appealed to the Circuit Court of Appeals for the Eighth Circuit and is reported as Schlafly v. U. S., 4 Fed., 195, wherein the decision of the District Court was affirmed.

It would seem to us that we must give these same words used in the exemption provisions of the 1921 Act some material, reasonable construction or else we must assume that Congress intended that they should be construed arbitrarily. If they are to be construed arbitrarily it presents indeed a difficult task requiring the selection of some particular percentage or proportion, such as more than a half, seventy-five per cent, ninety five per cent or it may be ninety-nine per cent. If, however, we consider the subject-matter and endeavor to reach some conclusion as to what was reasonably intended, our duty becomes something more than that of making a selection or drawing in a lottery.

Of course, in due time all of these associations became aware of the provisions of the new law, so that within a few months after the advent of the new ex-

emption provision it became a very simple matter for all of them to comply therewith and, except for the year 1922, the question now under discussion is purely academic. All that was necessary to be done after the provisions of the new law became known was for associations to require all borrowers to become members by subscribing to stock. (See Acklin *v.* Peoples Savings Association, 293 Fed., 292.)

III.

Is the Year 1921 Controlled by the 1918 or 1921 Act?

While no argument was made on this subject in the brief of the Government it has assumed that the 1921 Act controls the year 1921. This we dispute.

As we have heretofore shown, all Acts prior to the 1921 Act exempted these associations without condition, so that they were not required to confine their loans to members in order to be exempted until the 1921 Act was passed. The 1918 Act was in full force and effect until November 23, 1921, only five weeks before the end of that year, and up to that moment associations could not be denied exemptions upon the ground that they made loans to others than members. When, on November 23, 1921, Congress enacted the 1921 Act did it intend by any provision of the exemption clause to take away that which had already been granted, or did it intend prospectively in respect of the exemption clause to limit it to associations who in the future confined their loans substantially to members?

The 1921 Act provided at Section 231(4) that building and loan associations which confine their loans substantially to members shall be exempt from taxation under that Act. No language can be found in the entire exemption section indicating an intention to take away an exemption which had already vested in these associations up to the passage of that Act. The only reason for the assumption indulged in by the Government is to be found in Title XIV relating to repeals, where, at Section 1400, it was provided that Title II (relating to income tax) of the Revenue Act of 1918 is repealed as of January 1, 1921. This, we say, Congress intended to relate only to those who by the terms and the provisions of the 1918 Act were *subject to the tax* and not to those which had been exempted up to the date of the passage of the 1921 Act. This seems clear in view of paragraph (*b*) of Section 1400, which continues the 1918 Act in force, for the assessment and collection of all taxes which have accrued under that Act (as to those *subject* to the tax) at the time such parts of the Act which are repealed cease to be in effect.

The scheme evidently intended was that in respect of those subject to the tax, the tax imposed by the 1921 Act shall be in lieu of the tax imposed under the 1918 Act except where taxes had accrued under the 1918 Act at the time the 1921 Act was passed. Many corporations may have had a fiscal year ended prior to the passage of the 1921 Act, but subsequent to January 1, 1921. Consequently the 1921 Act could not operate upon them until the beginning of their next fiscal year,

because in such cases the taxpayer's liability had already accrued and could not be retroactively changed by the provisions of the subsequent Act, or at least such was not the intention of the Act.

To give this exemption provision of the 1921 Act retrospective meaning would be to say that Congress did not intend that any building and loan association should be exempted for the year 1921, because, having properly made loans to others than members under the 1918 and prior Acts up to November 23, 1921, they would be powerless to recall those loans back to January 1, 1921, in order to comply *nunc pro tunc* with the retrospective provision of the 1921 Act. Thus we say Congress merely intended, so far as the exemption was concerned, that associations must comply with the provisions of the 1921 Act from and after its passage.

This Court has expressed itself in no uncertain terms concerning retrospective legislation, notably in the case of Shwab *v.* Doyle, *supra*, and more recently in the case of Nichols *v.* Coolidge, 274 U. S. 531. We contend, therefore, that there was no intention of Congress to retrospectively deny exemption and that the retrospective operation of the repeal provision related only to those who were subject to the tax; but if any intention to the contrary can be found then we say that the Congress was without authority to take away the exemption which had been granted up to November 23, 1921.

The Court of Claims, in its opinion (R. 12), agrees with our construction, stating:

> "The Act of 1918 is applicable to the years 1918, 1919, 1920, and from January 1 to November 23, 1921; and the Act of 1921 is applicable to the period between November 23 and December 31, 1921, when the act was passed, and to the years 1922 and 1923."

Again in its opinion (R. 17) it stated:

> "The Act of 1921 exempting only such associations as confined their loans substantially to members could not affect the legal status of associations operating prior thereto and under other acts which did not even require the filing of a tax return. In attempting, after the passage of the 1921 act, to enforce the collection of taxes under prior acts the Commissioner of Internal Revenue was evidently under the impression that the exemption under the prior acts was likewise intended only for associations whose business was substantially confined to loans to members. The 1921 act is not susceptible of this construction. It was operative only upon the business of such associations after the effective date of the act. It should be stated in this connection that since the passage of the 1921 act plaintiff company has substantially complied with its provisions."

So it is that unless this construction be correct, we must conclude, without any apparent reason, that the Congress intended retrospectively to take away the exemption of all building and loans associations for one single year, namely, the year 1921. Such an intention is repulsive to the history of the entire legislation.

Let us now briefly reply to such points raised in the Government's argument as may not have been fully covered herein.

On page 5 of its brief there is set forth the proportion of the deposits on hand on the last day of each year to the total assets of the association on the last day of each year. We fail to see what that has to do with the issue, since all associations have the right to accept deposits, and the amount which they may accept is governed entirely by the amount they are able to lend. Consequently, an association which accepts deposits in excess of the amount it is able to lend would soon go out of business. Practically all the associations accept deposits; the Ohio laws permit this association to accept deposits; the text book writers all maintain that they have authority to do so unless prohibited by statute; and the decisions of the courts uphold the practice. It has also been seen that up to the time of the enactment of the 1921 Act it was entirely proper for associations to make loans to others than members; the Ohio laws permitted this association to do so; all text book writers hold it to be within their powers unless specifically prohibited by the laws of the State which created them; the Departmental Regulations permitted it; and there is no decision of any court which holds to the contrary.

It should be noted that in order to endeavor to swell percentages the Government has denominated as a loan to a nonmember money which the association had deposited in a bank or deposited with other building and loan associations. One who deposits money in a

bank is not usually deemed to have made a loan, and certainly not the kind of loan which building and loan associations are accustomed to make.

The Court of Claims observed (R. 14) that this association made 40 mortgage loans to members and 39 to nonmembers in 1918; 158 to members and 47 to nonmembers in 1919; 143 to members and 70 to nonmembers in 1920; 177 to members and 30 to nonmembers in 1921; 175 to members and 10 to nonmembers in 1922; and 262 to members and one to nonmembers in 1923. Through the entire period 1918 to 1923 the Court of Claims points out that 955 mortgage loans were made to members and 197 to nonmembers. And for the entire period 1918 to 1923, the court points out that the total loans were $2,271,604.40, of which $1,488,294.28 was loaned to members and $783,310.12 to nonmembers. Thus, as the court shows, 82 per cent of the total number of loans made during the whole period was to members, and 18 per cent to nonmembers, and in respect of the total amount loaned during the whole period 70 per cent thereof was to members and 30 per cent to nonmembers, which includes the years 1918 to 1921, when the law permitted the making of loans to nonmembers.

It should also be borne in mind, as the Court of Claims has pointed out (R. 17), that since the passage of the 1921 Act this association has substantially complied with its provisions, and as shown by Finding VIII (R. 10) for the two years controlled by the 1921 Act, namely, the years 1922 and 1923, the association made 452 loans to members and 74 loans to nonmem-

bers, or 95 per cent to members; and of the total loaned in these two years $919,072.33 was to members and $124,075 to nonmembers, or approximately 90 per cent to members.

It will also please be observed (Finding VIII, R. 10) that for the entire period 1918 to 1923, 1,291 loans were made, of which 1,089 were mortgage loans on homes, farms and real estate, or 90 per cent, while only 302 were business and collateral loans and loans to churches and on apartments.

It should also be noted that at the end of the year 1923 this association had, after forty-five years in business, only $29,106.69 cash on hand, including all undivided profits, indicating that it has paid to its members for the past forty-five years practically every dollar of its earnings in the form of dividends to offset the interest payable by them on their loans and thus has enabled them at the lowest possible cost to own their own homes. No other institution in the world could boast of such a record, nor could such business be transacted for the benefit of the home owning citizen by any other class of institution in this country; and yet, notwithstanding this record and that this association has been doing business as a domestic building and loan association in the State of Ohio for forty five years without question, you are asked now to find that it is not a building and loan association and that it is operated solely for private gain or profit.

What Kind of Association Did Congress Intend to Exempt.

To sustain its contention that this association does not measure up to the standard of a building and loan association, the Government (page 9 of its brief) cites Sections 3, 7 and 17 of Sundheim on the Law of Building and Loan Associations; Sections 1 and 7 of Endlich on Building Associations; Sections 920 and 921 Corpus Juris; 4 R. C. L. 343; and Eversman v. Schmitt, 53 Ohio State 174. *Inter alia*, we rely upon the same authorities, except the last, to support the opposite contention. As to the last (Eversman v. Schmitt), we will prove it to be inapplicable.

Section 3 of Sundheim on Building and Loan Associations describes the original building and loan association as it first sprung up in this country and to a large extent what is there stated is applicable to associations operating today. Section 7 is quite applicable to these associations as they exist today. We fail to see what comfort, however, the Government can find in citing this section, for we find therein the following:

> "They are the savings bank of the small investor, and their adaptability for that purpose has been fully demonstrated. They offer the best plan yet devised for people of small means to secure their own homes and for systematic saving of small sums of money. They are the most economically conducted financial institutions in the world, and have, despite this, suffered the least financial loss. They have grown to such an extent in recent years that they no longer restrict their money to the home buyer,

but loan their money to the mere investor or dealer in real estate. They are the holders of large mortgages secured upon farms, factories and other business properties and rows of stores and dwellings. This is not an abuse of their powers or a departure from their main purposes, but only a natural and proper expansion along healthy and legitimate lines. All legislation in recent years has been to enlarge and broaden their powers, not to confine and restrict them. The courts have been liberal in the construction of these especially delegated powers, and, as a result, they have grown and changed as conditions required. Judge Endlich, no doubt the greatest authority on these institutions, well says: 'It is, indeed, to be noted that the legislature has attempted no definition of what constitutes a building association. It has assumed that certain features and methods are essential to it, and there is no room for doubt that without them no corporation, whatever its label, can claim to be a building association. But it has not excluded the possibility that, consistently with these essential features, the legitimate development of the business of these associations may add others which, at the date of enactment, were not foreseen and against which, therefore, it is not to be taken as implying any prohibition.'"

Section 8 of this work treats of the benefits such associations are to a community and Sections 9 to 15 give illustrations of seven different methods of operation. Section 190, dealing with the subject of taxation, gives us an idea of the reasons why these associations should be exempt from taxation.

The Government finally cites one more Section, being Section 17. There is nothing in this section that is foreign to any building and loan association in the State of Ohio, and certainly not to the case of this respondent.

Permit us now to direct your attention to a few other sections contained in this work of Mr. Sundheim dealing more directly with the matter in dispute.

At Section 9, page 25, the author deals with different plans of associations as they exist and operate under different State statutes.

At Section 111, page 112, the same author states:

> "Loans are made for the purpose of purchasing a homestead, or *other real estate, or for any lawful purpose or business, but there is no duty or obligation of the association to inquire for what purpose the loan is obtained, or to require any stipulation upon the borrower as to what use he will make of the money, or in any manner to supervise or control its disbursement.*" (Italic letters supplied.)

The Government (page 9 of its brief) next cites Sections 1 and 7 of Endlich on Building Associations. We have already quoted (*supra*) from that authority in respect of the matter of the authority of these associations to make loans to nonmembers (Sec. 313).

At Section 1, Judge Endlich, writing in 1882, furnishes us with an introduction to the subject of his treatise and at Section 7 he gives us an insight into the general scheme of operation of the original building association, none of which is questioned.

We have already quoted from Section 313 dealing with loans to nonmembers and we now refer to Section 77 dealing with the matter of accepting deposits, where the author states:

> "There is, where it is permitted by law to exist, a class, known as 'depositors,'—persons who, without entering the circle of the society's membership, and becoming liable to all its duties, and sharing in all its benefits, use its treasury as a savings bank, in which to deposit, from time to time, small sums of money, with the privilege of drawing them, at their pleasure, thereafter under certain restrictions, and with the addition of interest at a certain moderate rate. These people are not members. Their status depends entirely upon statutory provisions; for, without such, the society has no right to take their money, and the safety of their own deposits is materially imperiled."

The right of this and other associations in Ohio to accept deposits is regulated by the Ohio General Code, in effect during the entire period here involved—Section 9648. (See Appendix.)

Attention is invited to Section 311 of Endlich on Building Associations, where the author deals with the manner in which associations may invest their funds, and compare this with the rigid restrictions of the Ohio laws in regard thereto. (See Ohio laws, Secs. 9660, 9661, 9662—Appendix.)

The Government next cites 9 *Corpus Juris*, 920, 921. These sections deal with the origin and growth of these associations and their history wherein there is

portrayed only the original purpose and scope of authority of these associations.

We now invite attention to 9 *Corpus Juris*, 922, where we find the following:

> "The main features of the plan of the ordinary building associations have already been set out in the definition" (this is what the defendant has quoted), "and in some cases the courts have described with more or less detail the plan and mode of operation of such associations and societies; but while the general plan and purpose of all such associations is the same, yet *because statutory regulations are meager in some States and abundant and detailed in others, their methods of transacting business are by no means uniform*, and the decisions of the courts passing on their transactions are far from being harmonious. Also the character of mutuality required is not always the same under different statutes."

We also invite attention to page 923, Section 8, which states:

> "While building and loan associations originated at an earlier date, it was not until about the middle of the nineteenth century that the States generally enacted statutes authorizing their incorporation, granting them privileges, and regulating their business. By virtue of its police power the State may regulate building and loan associations even to the extent of limiting the carrying on of their business to incorporated associations or to the extent of making the State auditor a general supervising officer over this class of corporations."

We also call attention to page 954, Section 70, where we find that where there is express statutory authority, a building and loan association may make loans to nonmembers, and may, unless its power is restricted by statute, loan money for other than building purposes, and that it is not required to ascertain the use to which a borrowing member intends to apply the money.

Next the Government cites 4 R. C. L., 343. Section 2 thereof relates to the building society as it was first organized and the author's of that work follows in general what all of the other authors herein referred to have stated and to which there is in general no criticism whatever. We direct attention, however, to the last sentence of Section 2, which is as follows:

> "In arriving at a determination of the question whether a particular corporation is a building and loan association the name of the association is not material, if it has *the purposes and characteristics named in the statute authorizing the organization of such an association.*"

Finally, at page 9 of its brief, the Government cites Eversman v. Schmitt. This case was decided by the Ohio State Court June 11, 1895, at a time when the laws of the State of Ohio did not permit building and loan associations to make loans to any but members. So long as that remained the law of Ohio that case may be appropriately cited, but on May 11, 1908, thirteen years later, the Ohio legislature passed what was known as the "Russell Bill," which was the law of Ohio during all the years involved in this controversy

being set forth in full in the Appendix hereto. That law permitted associations to make loans to members and others and to accept deposits from members and others and this has been the law of Ohio for the past twenty years. The case cited, therefore, is not applicable as a test of what is a building and loan association in Ohio at any time subsequent to the year 1908. It seems remarkable but true that the Government cannot find a single case arising in the State of Ohio subsequent to the year 1908 which holds that an association in that State lending to or accepting deposits from others than members is not a building and loan association. The laws of Ohio since February 21, 1867, being the first statute dealing with the incorporation of these associations, have permitted them to receive deposits either from members or nonmembers.

The Government's position is that notwithstanding the Congress has exempted *domestic* building and loan associations and has defined "domestic"; and that the respondent is such an association under the Ohio laws; nevertheless it is not a building and loan association according to common usage of the term in this country. The best answer to that is the history of these institutions. However, the real question here is what did Congress intend as may be determined by the rules of statutory interpretation.

History of Building and Loan Associations in the United States.

We will now very briefly discuss the origin and history of this character of association as it has been

known in this country, assuming that Congress in exempting building and loan associations intended to exempt them as they were known to exist and operate in the various States of the United States, since, at the time of the enactment of the Revenue Act of 1918 and for at least fifty years prior thereto, there did not exist in the United States such a thing as a common law building and loan society. All of them, ever since at least fifty to seventy-five years before the passage of the act, owed their entire existence, including the scope of operations or methods of doing business, to the statutes of the various States enacted in respect of such associations. Associations so created and operating were the only institutions that Congress could have intended its act to operate upon because there were no other associations of the kind in this country, except those created by State statute. Congress, no doubt at the suggestion of the Treasury Department, in 1921 decided that it would no longer allow building and loan associations as they existed in the various States to be exempted, but placed one restriction only upon them. This permitted them to be exempted if they were a building and loan association under the State laws, provided, after that act became effective, substantially all of their loans were made to members. It must follow, then, as we will fully demonstrate, that until Congress placed this restriction upon exempting these building and loan associations as they existed in the States for years, where they have been exempted under every revenue act that has ever been passed, they must be given exemption up to the passage of the 1921 Act without restriction.

The first building and loan association was established in 1815 by the Earl of Selkirk, in Scotland, and the first one in the United States was organized in Brooklyn, New York, in 1836. Their growth and extension have been rapid, both in Great Britain, where an act of Parliament in 1836 greatly facilitated their formation and control, and in the United States, where they now exist in one form or another in nearly all the States. As originally created, more than one hundred years ago, not by any statute but simply by the organization of individuals, they were intended by small periodical payments to permit people of limited means to become the owners of homes, and thereby thrift, economy and good citizenship was promoted. (See 9 *Corpus Juris*, 921.) The underlying purpose, therefore, was to enable people of limited means who did not have the ready cash to be able to acquire *homes* and thereby to promote thrift, economy and good citizenship. But while the general plan and purpose of all such associations is the same, yet because statutory regulations are meager in some States and abundant and detailed in others, their methods of transacting business are by no means uniform. (9 *Corpus Juris*, 922, citing numerous cases.)

There were associations known as "terminating societies," which, by their rules, are to terminate at a fixed date or when a certain specified result is attained. This character of association does not now exist in the United States. Can we infer that Congress intended its act to relate to such a thing? There was another class, known as "serial associations," where its stock is divided into series, each series being issued

separately and maturing separately, the intervals between the issues being determined by the money on hand or by the rules of the association, and the profits or losses were generally reckoned on the whole stock and then divided equally among the different series, unless the rules provide otherwise. This kind of building and loan associations does not generally exist in the United States.

Did Congress have these in mind?

Another class is known as "the permanent association," being one which issues its stock, not all at once, nor in series, but at any time when application is made therefor, and therefore one may become a member in a permanent association at any time without any back payment of dues. This is the character of association which generally exists in this country, as modified, however, by statute in the various States. In England a permanent society is one which has not by its rules any fixed date or specified result at which it shall terminate.

It is said that while building and loan associations originated at an earlier date it was not until about the middle of the nineteenth century that the States generally enacted statutes authorizing their incorporation, granting them privileges and regulating their business. By virtue of its police power a State may regulate building and loan associations even to the extent of limiting the carrying on of their business to incorporated associations or to the extent of making the State auditor a general supervising officer over

this class of corporation. In the exercise of this power various statutes have been passed relating, among other things, to the incorporation of such societies, to their powers, to the withdrawal of stockholders and to the imposition, amount and collection of dues, fines, premiums and interest. Some of these statutes are by their terms applicable only to such associations as elect to do business thereunder, while many others regulate only foreign associations (9 *Corpus Juris*, 923D).

We also find that, in the *absence* of a statute expressly authorizing the creation of such associations, building and loan associations may be organized as voluntary associations or formed into certain corporations under the general law; but where there is a general provision for the incorporation of such societies they must be organized thereunder, and except in a very few jurisdictions where unincorporated societies have existed, the general practice requires incorporation. (See 9 *Corpus Juris*, 924A.)

It will readily be seen, therefore, that Congress could not have intended its act to relate to something which did not exist, namely, the original building and loan association, which was an unincorporated affair and which did business in an old-fashioned way not known now and not known in this country for the past seventy-five years. It must also appear, at all events, that since under the laws of all the States in the United States these associations are required to be incorporated and all of them to be regulated and controlled by a public official, whose duty it is to see that they operate and

conduct their business within the provisions of the laws of the State creating them, that this is the only kind of association Congress could have intended because no other kind existed in the United States. If that be true, by what authority does the Commissioner attempt himself to impute to Congress what *he* regards as a true building and loan association? Can he select from the States one whose laws in respect of building and loan associations seem to coincide with his particular idea of what a building and loan association should do and how it may operate and then say that Congress intended only to exempt *this* kind of association? Was any such power conferred upon him, or must he accept these associations as they have existed in the States, and particularly in the States of Ohio, for the past forty or fifty years and exempt them until and unless Congress shall either define the kind of building and loan association it intends to exempt or else until and unless Congress, while accepting these associations as they exist in the various States, shall prescribe some restriction upon their exemption which shall apply to all alike? Until the passage of the 1921 Act Congress accepted these associations as they existed in the various States. In 1921, as we have already pointed out, Congress undertook for the first time to place a restriction upon their exemption, and in doing so it accepted them as they existed in the States, provided that, regardless of the powers conferred upon them by the States, they confine their business to making loans to members.

The evidence in this case shows beyond a shadow of doubt that this association which has been steadily engaged in business for forty years as a building and loan association, known to everyone as such, has complied with all the laws of the State of Ohio, and since the creation of a superintendent of building and loan associations by that State, in the year 1891, it has been annually inspected and has received a certificate each year to the effect that it has complied with the Ohio laws relating to the conduct of the business of a building and loan association in that State. This answers the requisites of the Revenue Act of 1918, which governs the years 1918, 1919, and 1920 and until the passage of the Revenue Act of 1921, on November 23 of that year. We concede that when the 1921 Act was passed in order to be exempt this association must do one thing more than comply with the laws of the State of Ohio relating to the carrying on of business of a building and loan association, and that is it must confine its business *substantially* to the making of loans to its members. The evidence shows that from December, 1921, shortly after the passage of the Revenue Act of 1921, throughout the years 1922 and 1923, which are the only subsequent years in controversy, substantially all of its business was confined to making loans to its members, since 90 per cent of its loans in those two years were to members and 87 per cent of the money loaned was to members. (See years 1922-1923, Finding VIII, Rec. 10.)

The government on page 12 of its brief cites *Lilley Building & Loan Company* v. *Miller*, 285 Fed., 143,

also on page 14 *Appeal of Johnstown Building & Loan Association*, 6 B. T. A., 462, and *Broadview Savings & Loan Company v. Commissioner*, 10 B. T. A., 725.

The Lilley Case.

This case was cited by the government on page 12 of its brief as authority for its contention that the words "without capital stock organized and operated for mutual purposes and without profit," contained in the exemption provisions of the 1916 and 1918 Act, modifies "domestic building and loan associations" as well as "co-operative banks." For convenience, we repeat the exemption provision of those acts:

> "SEC. 231. That the following organizations shall be exempt from taxation under this Title—
>
> "4. Domestic building and loan associations *and co-operative banks without capital stock organized and operated for mutual purposes and without profit.*"

We have heretofore shown in the history of the legislation that after the 1916 Act had been passed by the House, exempting domestic building and loan associations, the Senate and the Conference Committee agreed to extend the exemption to another institution and as stated therein the purpose of the amendment was to exempt also "co-operative banks without capital stock organized and operated," etc. It is quite apparent, therefore, that this had nothing to do with the exemption of building and loan associations, as the Court of Claims has pointed out. Furthermore, no one ever heard of a building and loan association with-

out capital stock, but co-operative banks have no capital stock; and building associations are operated for profit, for the benefit of their members, whereas co-operative banks are not operated for profit. Furthermore, it is an elementary rule of grammar that a phrase or clause modifies only its immediate antecedent.

Attention is invited to the fact that the Lilley case was not decided until after the passage of the 1921 Act but it interprets the 1916 and 1918 Acts. We have pointed out the history of all legislation prior to the 1921 Act, together with the executive construction and judicial interpretation thereof, from which no doubt could be entertained of the intention of Congress when it passed the 1918 Act. It would, therefore, be incompetent four years later for any court, after the passage of a subsequent act, to place some other interpretation upon this intention. In fairness to Judge Peck, who decided the Lilley case, but who is no longer on the Bench, we wish to point out several fundamental errors in his decision of that case, due, perhaps, to the fact that the decision was based upon totally mistaken premises, to which his attention may never have been directed.

First, he proceeded upon the assumption that the 1909, 1913 and 1916 Acts were identical, whereas we have clearly pointed out that the 1909 Act contained a restrictive clause which was deliberately stricken out in the 1913 Act and never appeared in the subsequent acts.

Next, his opinion is based upon the decision in the case of *Eversmann v. Schmitt* (*supra*), which, as we have pointed out, was a decision rendered in 1895, at a time when Ohio associations were not permitted to make loans to others than members.

Next, Judge Peck relied upon the case of *Hadsell v. Union Ins. Co.*, 105 Miss., 268, which dealt solely with the interpretation of the Mississippi Constitution. In that case the court ordered a rehearing (page 280 of the opinion) and reversed its former decision, from which Judge Peck quoted and upon which he relied.

Next Judge Peck erroneously interpreted the words "without capital stock organized and operated for mutual purposes and without profit" in the exemption provisions of the 1918 Act as modifying "domestic building and loan associations," as we have pointed out.

Next it appears that Judge Peck was unaware that in 1917 Congress passed a special act ordering the refund of all taxes collected from these associations as having been illegally collected even under the stringent provisions of the 1909 Act.

We must assume that had Judge Peck not been mistaken in his premises and had he been aware of the errors upon which his decision was founded he would have reached the opposite conclusion, if he would have applied the established principles of statutory interpretation. It is only fair, however, to say that perhaps the most unusual facts which were before him in the Lilley case probably had a great deal to do with his ultimate conclusions, but we do not agree from a

legal viewpoint that even these facts should have affected his conclusions. A casual reading of the facts in the Lilley case indicates beyond question that it can scarcely be considered a precedent for any other case. The Court of Appeals affirmed the decision in the Lilley case without opinion, being evidently unaware of the fundamental errors which we have pointed out.

The Eccentric Facts in the Lilley Case.

While there are many facts of a general nature appearing in connection with the Lilley case that are applicable to all associations, yet there are several outstanding facts in that case which are not applicable to the case of any other association which has been presented for judicial determination. We will discuss, therefore, only these eccentric facts, because the court's decision must be due to them or else it must be said to have opposed the reasoning of every other court which has ever considered the principles involved in these cases. What are these facts?

First, it received deposits of nonmembers *evidenced by entries in books such as are ordinarily used by savings banks*. The style or character of the book of itself should not be of any great importance, but it probably received the consideration of the court.

Second, out of all of the loans made by the Lilley Building & Loan Association for the typical year considered by the court, only *two* were to stockholders or members of a total of four hundred ninety-five (495). In other words, only four-tenths of one per cent of its loans were made to members. That is the outstand-

ing feature of the Lilley case and that was the reason, if any there be, why that association was held not to be exempt. Upon this point the court in the Lilley case observed:

> "It is not thought that the making of loans to nonmembers or borrowing from nonmembers, or receiving deposits to be withdrawn on demand or on time, so long as such transactions are simply incidental to the primary purpose of operating a mutual building association, would defeat the exemption."

And further in its opinion, and with which the court concludes its observations upon the facts, we find:

> "It may not be possible to define precisely how far a building association may go in extraneous activities without losing its essential character, but it seems clear that when it ceases to be substantially mutual and adopts *as its chief business dealing for profit with the general public by the methods of an ordinary savings bank*, it is no longer a building association *entitled to be exempted* from income taxation under the statute in question."

The Court of Claims has very thoroughly reviewed the Lilley case and reached the inevitable conclusion that in principle it was fundamentally unsound in attempting to revive a dead issue, namely, the meaning of the 1918 Act, which, theretofore, had never had but one meaning, one executive construction and one interpretation by the courts, interpreting the prior statutes *in pari materia*.

The Johnstown case (*supra*), decided by the Board of Tax Appeals, involved the 1918 Act and the 1921

Act. The Board exempted that association for the year 1922 under the 1921 Act, but held it not exempt under the 1918 Act, using as its sole authority the decision in the Lilley case, without any reference to the history of the legislation, the executive construction, or the interpretation of the prior statutes, and without any reference whatever to the laws of Ohio, and notwithstanding the Johnstown association was admittedly a building and loan association under the laws of Ohio.

In the case of the Broadview association (*supra*), cited by the government, the years involved were controlled by the 1921 Act. There the Board in effect overruled its decision in the Johnstown case for the year 1922, where the facts were almost identical, and applied an unheard of principle of reasoning, which we will briefly set forth.

The facts in the Broadview case were that all of the loans made by the association were to members exclusively since the passage of the 1921 Act limiting exemption to associations which confined their loans substantially to members, but because in prior years *long before the passage of the 1921 Act* the association had made loans to others than members, which loans had not been completely repaid and upon which payments were still being made during the taxable year 1922, together with interest, the Board held that the receipt after the 1921 Act of such interest and payments on loans made many years prior thereto to nonmembers, being no part of the business done in 1922, constituted such business with nonmembers as to deprive it of exemption for the year 1922.

The proposition amounts to no more than this: Although an association after the passage of the 1921 Act confined its loans substantially or entirely to members, yet it is not entitled to exemption if there be found on its books outstanding loans which had been made within ten years prior thereto to others than members and upon which payments on such loans with interest were being made. This means, in effect, that if an association permits the repayment of those old loans with interest after the passage of the 1921 Act it prevents exemption. In other words, to be exempt after the passage of the 1921 Act, it would be necessary for an association to cancel all outstanding loans which may have been made from one to ten years prior thereto to others than members or else forfeit its exemption. Did Congress have in mind any such absurd intention? If it did then it did not intend its act to benefit any association, because all of them in the State of Ohio, and in most of the States prior to the passage of the 1921 Act, had the right to make loans to nonmembers and to accept deposits from them, so, naturally, upon the passage of the 1921 Act they had outstanding on their books unpaid loans as well as deposits. A building and loan association is a money lending institution and its business is making loans. What Congress meant was to confine that business in the future to loans to its members and it did not intend as a prerequisite to exemption thereafter that every association must immediately remit all deposits which it had prior thereto received from others than members and cancel all loans that had been made in the past to nonmembers.

It also appears that the Board was displeased because some of the loans made to *bona fide* members were used for other purposes thereafter by the individual. The Act places no such limitation upon exemption. (See Sundheim on Building and Loan Associations, 2nd Ed., p. 20, 22, 24, and p. 112, Sec. 111.)

Finally, on page 13 of its brief, the government refers to the case of Pacific Building & Loan Association *v.* Hartson, 201 Fed. 1011. This case is not only contrary to Parkview Building & Loan Association *v.* Herold (*supra*) and Central Building, Loan & Savings Co. *v.* Bowland (*supra*), subsequently decided, but in the latter case the fundamental error committed by the court in the case of Pacific Building & Loan Association is pointed out with unmistakable clarity.

In conclusion, we think that the very masterly, clear, and logical opinion of the Court of Claims is absolutely correct, sound, and a wholesome interpretation of the law involved, and its decision should be affirmed. Congress has the power to take away this exemption entirely at any time and certainly has the power from time to time to place such other and further restrictions upon exemption as it may deem advisable. Until it shall do so we think it is not within the province of the courts to undertake to regulate the exemption of these associations.

Respectfully submitted,

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October, 1928.

APPENDIX.

Laws of Ohio Relating to Building and Loan Associations.

Interpretation of Terms.

Sec. 9643. A corporation for the purpose of raising money to be loaned to its members, and others, shall be known in this chapter, and in the laws relating to the bureau of building and loan associations, as a "building and loan association," or as a "savings association." Associations organized under the laws of this state shall be known as "domestic" associations, and those organized under the laws of other states or territories, as "foreign" associations. Associations may be organized and conducted under the general laws of Ohio relating to corporations, except as otherwise provided in this chapter. (99 v. 528 1.)

Name.

Sec. 9644. The name of every such corporation hereafter organized, or heretofore organized and hereafter changing its name, shall begin with any word it may select, and end with the word "company" or with the word "association." It also shall use its name in any order it designates, and if it so desires, with other words not forbidden by law, any one or more of the following words, or combination of words, at its option: "Savings", "building", "loan", "savings and loan", or "building and loan." But such association shall not use the words "bank", "banking" or "trust" nor any one or more of them in combination. (99 v. 528 2.)

When Business May Be Commenced.

Sec. 9645. The capital stock named in the articles of incorporation shall be deemed to refer to the authorized capital. The organization may be completed and business commenced when five per cent thereof is subscribed, and the names and addresses of its officers and not less than two copies of its constitution and by-laws have been filed with the inspector of building and loan associations. (99 v. 528 3.)

Directors, Term of Office.

Sec. 9646. Directors may be elected for any term, not less than one year nor longer than three years. If such term be longer than one year, it shall be so arranged that as nearly as may be, the term of office of an equal number of directors will expire each year. (99 v. 528 4.)

Powers.

Sec. 9647. Such corporation shall have all the powers set forth in the following sections of this chapter. (99 v. 528 5.)

Receiving of Deposits; Joint Accounts.

Sec. 9648. To receive money on deposits, and all persons, firms, corporations and courts, their agents, officers and appointees may make such deposits and stock deposits, but such corporation shall not pay interest thereon exceeding the legal rate. When such deposits or stock deposits are made to the joint account of two or more persons, whether adults or minors, with a joint order to the corporation that such deposits or any part thereof are to be payable on the

order of any one or more of such joint depositors, and to continue to be so payable notwithstanding the death or incapacity of one or more of the persons making them, such account shall be payable to any one or more of such survivors or survivor or order notwithstanding such death or incapacity. No recovery shall be had against such corporation for amounts so paid and charged to such account. (99 v. 528 6.)

Issue of Stock: Vote.

Sec. 9649. To issue stock to members on such terms and conditions as the constitution and by-laws provide. Each member may vote his stock in whole or fractional shares, as the constitution and by-laws provide, but no person shall vote more than twenty shares in any such corporation in his own right, nor have the right to cumulate his votes. But every subscriber for stock in accordance with the constitution of the association, may vote the amount of stock so subscribed for, in no event to exceed twenty shares. (99 v. 529 7.)

Assessments.

Sec. 9650. To assess and collect from members and others, such dues, fines, interest and premium on loans made, or other assessments, as may be provided for in the constitution and by-laws. Such dues, fines, premium or other assessments shall not be deemed usury, although in excess of the legal rate of interest. (99 v. 529 8.)

Withdrawal of Stock Deposits.

Sec. 9651. To permit members to withdraw all or part of their stock deposits, at such times, and upon such terms as the constitution and by-laws provide.

Any member, however, who withdraws his entire stock deposit, or whose stock has matured, shall be entitled to receive all dues paid in and dividends declared thereon, less all fines or other assessments, and less the pro rata share of all losses, if any have occurred. (99 v. 529 9.)

Withdrawal of Deposits.

Sec. 9652. To permit withdrawal of deposits upon such terms and conditions as the association provides except by check or draft. But no such association shall be permitted to carry for any member or depositor any demand, commercial or checking account. Nothing in this chapter shall prevent members or depositors from withdrawing funds by non-negotiable orders. (99 v. 529 9.)

Cancellation.

Sec. 9653. To cancel shares and parts of shares of stock upon which the credits have been withdrawn, or upon which loans have been repaid, and re-issue them as new stock. (99 v. 529 10.)

Rules as to Minors.

Sec. 9654. To issue stock to minors and receive deposits thereon and permit both stock and deposits to be withdrawn, transferred, pledged and voted by such minors as other stock and stock deposits; to receive deposits of money by or for minors and to pay them to such minors, or upon their order. The receipt or paid order of such minor, therefor, shall be a valid acquittance of the rights of all concerned. (99 v. 529 11.)

Property, Leasing, Holding of.

Sec. 9655. To lease, acquire, hold, encumber, convey and rent such real estate and personal property as is necessary for the transaction of its business, or necessary to enforce or protect its securities. (99 v. 529-12.)

Borrowing Money.

Sec. 9656. To borrow money, not exceeding twenty per cent of the assets, and issue its evidence of indebtedness or other security therefor. (99 v. 530-13.)

Loans.

Sec. 9657. To make loans to members and others on such terms, conditions and securities as may be provided by the association. (99 v. 530-14.)

Cancellation of Loan.

Sec. 9658. To cancel such loans and release the securities on such terms as the board of directors provide. But any member may have his loan cancelled upon the following terms: After the premium for one year has been paid, and also the interest and premium up to the date of cancellation, the borrower shall pay the sum actually borrowed less the dues paid and dividends credited, and also any fines or other assessments required by the constitution and by laws. (99 v. 530-15.)

Reserve and Undivided Profit Fund.

Sec. 9659. To accumulate from the earnings a "reserve fund" for the payment of contingent losses, and

an "undivided profit fund", both of which may be loaned and invested as other funds of the association. (99 v. 530-16.)

Idle Funds, How Invested.

Sec. 9650. To invest any of its idle funds, or any part thereof, in bonds or interest bearing obligations of the United States, or of the District of Columbia, or of the State of Ohio, or of any county, township, school district, or other political division in the State of Ohio, or of any incorporated city or village, in the State of Ohio, and in such other securities as now are or hereafter may be accepted by the United States to secure government deposits in national banks. But such investments at no time shall amount in the aggregate to more than twenty per cent of the assets of such corporation. (99 v. 530-16.)

May Deposit Idle Funds.

Sec. 9651. To deposit any of such funds or part thereof, in any financial institution that is subject to inspection by the United States, or by the state of Ohio; and receive therefor certificates of deposit. (99 v. 530-16.)

Purchase Interest bearing Obligations, Sale of to Close Up Business Permitted.

Sec. 9652. To buy but not to sell, except whenever it desires to terminate and close up its business affairs or in case of financial emergency, and then only with the consent previously had of the inspector of building and loan associations, interest bearing obligations secured by real estate mortgages, which shall in all respect comply with, and be within the rules adopted

for making mortgage loans by the corporation making such investments. Such mortgage investments may be held and reported as mortgage loans. (106 v. 431.)

Distribution of Earnings.

Sec. 9663. To make such annual or semi-annual distribution of the earnings as is hereinafter provided, and as the constitution and by-laws may prescribe. (99 v. 530-17.)

Certificate of Increase, Decrease, etc., Where Filed.

Sec. 9664. To increase or decrease its authorized capital or the face value of its shares, or change the name of the corporation by a majority vote of its board of directors. A certificate of such action shall be made by the president and secretary, and duly filed with the secretary of state, after which in the use of the changed stock and changed name, all rights of all parties shall remain the same as before such change was made. (99 v. 530-18.)

Dissolution.

Sec. 9665. To dissolve the corporation when by a majority vote of the stock entitled to be voted under its constitution and by-laws, which shall be consistent with the provisions of section ninety six hundred and forty nine, its continuance is deemed to be no longer desirable, but subject to the contract rights of its borrowers, and the vested rights of its members. (99 v. 531-19.)

Amendment of Articles.

Sec. 9666. To amend its articles of incorporation, and increase or decrease the number of its directors, by complying with all the requirements provided in

its own constitution for the amendment thereof. The other officers of such corporation shall consist of a president, one or more vice presidents, one or more secretaries, and such others as its constitution and by-laws provide. (99 v. 531-20.)

Constitution and By-Laws.

Sec. 9667. To provide, by constitution adopted by its members, and by laws adopted by its board of directors, for the proper exercise of the powers herein granted, and the conduct and management of its affairs. (99 v. 531-21.)

Other Powers.

Sec. 9668. To have all such other powers as are necessary and proper to enable such corporation to carry out the purpose of its organization. (99 v. 531-22.)

Banks, Designation of, to Receive Funds.

Sec. 9669. The board of directors shall designate a bank or banks, in which it shall cause the funds of such corporation to be deposited in its name. Such funds when so deposited, can be withdrawn only in such manner and for such purpose as is provided in the constitution and by-laws and authorized by law. (99 v. 531-23.)

Bond of Officers.

Sec. 9670. All bank books showing such deposits shall be open to the inspection of any director at any time. All officers of such association who have charge or possession of moneys, securities, or property, shall give bond before entering upon their duties, to the satisfaction of the board of directors, for the faithful performance thereof, and the safe keeping and proper

application of all moneys or property coming into their hands. All officers of such corporations on being re-elected to office shall renew their bonds. The bond may be increased or additional securities required at any time by the board of directors. Directors shall not be eligible as bondsmen, but shall be individually liable for any loss to members, caused by their neglect to comply with the provisions of this and the preceding sections. (99 v. 531-23.)

Reserve Fund.

Sec. 9671. The amount to be set aside to the reserve fund, for the payment of contingent losses shall be determined by the board of directors, but in all permanent or perpetual associations, at least five per cent of the net earnings shall be set aside each year to such fund until it reaches at least five per cent of the total assets. All losses shall be paid out of such fund until it is exhausted. When the amount in such fund falls below five per cent of the assets as aforesaid, it shall be replenished by annual appropriations of at least five per cent of the net earnings as hereinbefore provided until it again reaches such amount. (99 v. 531-24.)

Expenses; How Paid.

Sec. 9672. All expenses of such association shall be paid out of the earnings only, and so much of the earnings as may be necessary must be set aside each year for such purpose. But charges incident to a loan, if paid by the borrower, shall not be deemed a part of the current expenses. (99 v. 532-25.)

Dividends.

Sec. 9673. After payment of expenses and interest, a portion of the earnings to be determined by the board of directors, annually or semi-annually, shall also be

placed in the reserve fund for the payment of contingent losses, as hereinbefore provided, and a further portion of such earnings to be determined by the board of directors, shall be transferred as a dividend annually or semi-annually, in such proportion to the credit of all members as the corporation by its constitution and by-laws provides, to be paid to them at such time and in such manner in conformity with this chapter as the corporation by its constitution and by-laws provides. Any residue of such earnings may be held as undivided profits to be used as other earnings, except that such undivided profit fund at no time shall exceed three per cent of the total assets of the association. (99 v. 532 25.)

Losses.

Sec. 9674. All losses shall be assessed in the same proportion and manner on all members after the amounts in the reserve fund and the undivided profit fund have been applied to the payment thereof. (99 v. 532 25.)

Listing of Shares for Taxation.

Sec. 9675. The shares and loans advanced to its members shall be exempt from taxation, except that shares of stocks upon which no loans have been made or money advanced by the company, shall be considered and held as credits. The members individually shall list for taxation the number of shares held by them, and the true value thereof in money, on the day preceding the second Monday in April each year, and they shall be assessed at such valuation for taxation and taxes as other property. (99 v. 532 26.)

Inspection.

Department of Building and Loan Associations.

Inspector of Building and Loan Associations.

Sec. 674. The governor with the advice and consent of the senate, shall appoint an inspector of building and loan associations, who shall serve for a term of three years. No such inspector of building and loan associations shall have any official connection with a building and loan association, or be interested in the business thereof, except as a stockholder. (103 v. 181 1.)

Bond, Oath and Approval.

Sec. 675. Before entering upon the discharge of the duties of his office the inspector of building and loan associations shall give a bond to the state in the sum of ten thousand dollars with two or more sureties or with a surety company authorized to do business in the state of Ohio, approved by the governor, conditioned for the faithful discharge of the duties of his office. Such bond, with the approval of the governor and the oath of office endorsed thereon, shall be deposited with the secretary of state and kept in his office. (103 v. 181 2.)

Duties of Inspector.

Sec. 676. The inspector of building and loan associations shall see that the laws relating to building and loan associations are duly executed and enforced. When a violation of a law relating to building and loan associations is reported to him he shall take, or cause to be taken, the testimony, under oath, of any and all persons supposed to have any knowledge of such violation, and cause such testimony to be reduced to writ

ing. If he be of the opinion that there is sufficient evidence, he shall cause the person suspected of such violation to be arrested and charged with such offense, and shall furnish the attorney general or the proper prosecuting attorney with the information obtained by him, the names of the witnesses and a copy of all material testimony taken in the case. (103 v. 181-3).

Deputies.

Sec. 677. With the approval of the governor, the inspector of the building and loan associations may employ from time to time, the necessary deputies, assistants, clerks and examiners, to assist him in the discharge of the duties imposed upon him by law. With such approval he may remove any such clerk or examiners at any time. (103 v. 182 4.)

Salary of Inspector.

Sec. 677 1. The salary of the inspector of building and loan associations shall be three thousand six hundred dollars, per annum, and shall be paid at the same time as the heads of other state departments. (103 v. 182 5.)

Salaries of Deputies, Assistant, etc.

Sec. 677 2. The inspector of building and loan associations shall fix the salaries of the deputies, assistants, clerks and examiners at such rates per annum as the governor shall approve. Upon vouchers approved by the inspector of building and loan associations, such salaries shall be paid by the treasurer of state, upon the warrant of the auditor of state. (103 v. 182 6.)

Expenses.

Sec. 677-3. The actual and necessary traveling expenses of the inspector of building and loan associations, and of the deputies, assistants, clerks and examiners, incurred in the discharge of their official duties shall be paid monthly by the treasurer of state, upon the warrant of the auditor of state. Vouchers therefore shall be fully itemized, approved by the inspector of building and loan associations, and countersigned by the auditor of state. (103 v. 182 7.)

Sec. 674-4. All expenses incurred by the inspector of building and loan associations, in the performance of the duties imposed upon him by law, including the salary of such inspector, his deputies, assistants, clerks and examiners, shall be paid from funds appropriated therefor. (103 v. 182 8.)

Seal.

Sec. 677-5. The seal of the inspector of building and loan associations shall be one and three-fourths inches in diameter, shall have engraved thereon the coat of arms of the state, and shall be surrounded by the words, "Inspector of Building and Loan Associations of Ohio." (103 v. 182 9.)

All Instruments Sealed With the Seal Received in Evidence.

Sec. 677-6. Every certificate or other instrument executed, or order made, by the inspector of building and loan associations, in pursuance of any authority conferred upon him by law, and sealed with the seal of his office, or copies thereof duly authenticated under such seal, shall be received in evidence in all courts of this state. (103 v. 182 10.)

Place of Office.

Sec. 677 7. The inspector of building and loan associations shall be furnished by the state with suitable rooms, at the seat of the government, for conducting the business of his office. (103 v. 182 11.)

Foreign Associations.

Requirements from Foreign Associations.

Sec. 678. Foreign building and loan associations doing business in this state shall conduct such business in accordance with the laws governing domestic associations. No foreign building and loan association shall do business in Ohio until it procures from the inspector of building and loan associations a certificate of authority to do business in this state after complying with the following provisions:

1. It shall deposit with the inspector one hundred thousand dollars, in cash or bonds of the United States or this state, or of a county or municipal corporation therein, satisfactory to the inspector.

2. It shall file with the inspector a certified copy of its charter, constitution and by-laws, and other rules and regulations showing its manner of conducting business together with a statement such as is required annually from all associations.

3. It shall also file with the inspector a written instrument, duly executed, agreeing that a summons may issue against it from any county in this state directed to the sheriff of the county in which the office of inspector is situated, commanding him to serve it by certified copy personally upon the inspector or by leaving a copy thereof at his office. The inspector shall mail a copy of any papers served on him to the home office of such association. (99 v. 533 31.)

Certificate of Authority to Do Business.

Sec. 679. When a foreign building and loan association has complied with the provisions of the preceding section, and the inspector is satisfied that it is doing business according to the laws of Ohio, and is in sound financial condition, he shall issue his certificate of authority to the association to do business in this state. Annually thereafter, upon filing the annual statement herein provided for, if the inspector is satisfied as herein provided, he shall issue a renewal of such certificate. (99 v. 533 32.)

Collection of Interest and Exchange of Securities.

Sec. 680. A foreign building and loan association may collect and use the interest on securities deposited as provided by law so long as it fulfills its obligations and complies with the laws of this state. It may also exchange them for other securities of equal value satisfactory to the inspector. (99 v. 534 33.)

Securities Liable for Claimants.

Sec. 681. The deposit made by a foreign building and loan association with the inspector of building and loan associations shall be held as a security for all claims of residents of this state against such association, and be liable for all judgments or decrees thereon, and subjected to the payment thereof in the same manner as the property of other non-residents. Should an association cease to do business in this state, the inspector may release securities in his discretion, retaining sufficient to satisfy all outstanding liabilities. (99 v. 534 34.)

See also Section 178 of the General Code of Ohio.

Annual Reports.

Sec. 682. Every building and loan association doing business in this state, annually, at the end of each fiscal year or within forty days thereafter, shall make a full and detailed report in writing of the affairs and business of the association for the preceding year, and showing its financial condition at the end thereof. With the first report made by an association it shall file a certified copy of its constitution and by-laws, or other rules and regulations, showing its manner of doing business. (99 v. 534-35.)

Form of Report.

Sec. 683. The report required in the preceding section shall be the form and contain such information as is prescribed by the inspector of building and loan associations. It shall be sworn to by the secretary and its correctness attested by at least three directors or an auditing committee appointed by the board. The original shall be filed with the inspector of building and loan associations within forty days after the close of the fiscal year. Such an abstract therefore as the inspector requires shall be posted for sixty days in the office or meeting place of such association, and published in a newspaper regularly issued in the county in which it is located. (99 v. 534-36.)

Examination of Associations.

Annual Examination.

Sec. 684. At least once each year the inspector of building and loan associations shall make an examination into the affairs of each such association, or cause it to be made by a person appointed by him for that purpose. (99 v. 534-37.)

Expenses of Examination.

Sec. 685. The expenses of all examinations shall be paid by this state, except that when, by the laws of any other state, district, territory or nation, examinations of such associations of this state are required or permitted to be made by any official or other authority of such other state, district, territory or nation at the expense of such associations, then the expenses of all such examinations made by the inspector of this state, of such associations of that state, district, territory or nation, must be respectively charged to and collected from such associations so examined. (99 v. 534 37.)

Revocation of Charter for Illegal Practices.

Sec. 686. If upon examination, the inspector of building and loan associations finds any domestic association conducting its business in whole or part contrary to law, or failing to comply therewith, he shall notify the board of directors of such association of such fact in writing. If, after thirty days, such illegal practices or failure continue, he shall communicate the facts to the attorney general, who shall cause proceedings to be instituted in the proper court to revoke the charter of such association. (99 v. 535 38.)

Dissolution if Condition Unsound.

Sec. 687. If, upon examination, the inspector of building and loan associations finds that the affairs of a domestic building and loan association are in an unsound condition, and that the interest of the public demand its dissolution and the winding up of its business, he shall so report to the attorney general, who shall institute the proper proceedings for that purpose. (99 v. 535 39.)

Powers of Examiners.

Sec. 688. An examiner appointed by the inspector of building and loan associations, under the provisions herein relating to such associations, shall have access to and may compel the production of all books, papers, securities, moneys and other property of an association under examination. He may administer oaths to, and examine the officers and agents of such association as to its affairs. (99 v. 535-40.)

Inspector May Publish Result.

Sec. 689. If the inspector of building and loan association deems it to the interest of the public, he may publish the results of such examination in a newspaper of general circulation in the county in which such association is located, if it is a domestic association, and in some newspaper in the city of Columbus if it is a foreign association. (99 v. 535-41.)

May Cancel Authority of Foreign Association.

Sec. 690. If upon examination the inspector of building and loan associations finds that a foreign association does not conduct its business in accordance with law, or that its affairs are in an unsound condition, or if it refuses to permit an examination to be made, he may cancel its authority to do business in this State, and cause a notice thereof to be mailed to the home office of the association and published in at least one newspaper published in the city of Columbus. After the publication of such notice no such association or agent thereof shall receive further stock deposits from members residing in this state, except payments on stock on which a loan has been taken. (99 v. 535-42.)

Fees.

Fees to be Paid to Inspector.

Sec. 691. Foreign building and loan associations shall pay to the inspector of building and loan associations the following fees:

For filing an application for admission to do business in this State, five hundred dollars;

For each certificate of authority and annual renewal thereof, two hundred dollars.

Every building and loan association doing business in this State, whether foreign or domestic, shall pay to the inspector of building and loan associations, for filing each annual report, at the time said annual report is filed, the sum of ten dollars, and in addition thereto, one-eightieth of one per cent of its assets, as shown in such report. All such fees collected shall be paid into the general revenue fund. (106 v. 236.)

Securities to be Deposited With Treasurer of State.

Sec. 692. All securities or cash deposited with the inspector of building and loan associations shall be deposited with the treasurer of State, who, with his sureties, shall be responsible for the safe keeping thereof. The treasurer shall deliver such securities only upon the written order of the inspector. (99 v. 536-44.)

Dissolution or Consolidation of Building and Loan Associations.

Sec. 693. A building and loan association or a savings association may provide in its constitution and by-laws for the time and terms of its dissolution and for its consolidation with one or more of such corporations on terms and conditions to be determined

upon by their board of directors. In case of the dissolution of such a corporation, its board of directors by a majority vote may be authorized to sell and transfer its mortgage securities or other property, or both, to another corporation, person or persons, subject to the vested and accrued rights of the mortgagors. (99 v. 537-48.)

Penalties.

Forfeiture for Non-compliance.

Sec. 694. A building and loan association which does business in this State without first complying with the provisions herein or which violates or fails to comply with provisions of law relating to building and loan associations shall forfeit and pay not less than fifty dollars nor more than one thousand dollars, to be recovered by an action in the name of the State and on collection paid into the State treasury. (99 v. 536-45.)

Record of Proceedings of Inspector—Report.

Sec. 695. The inspector of building and loan associations shall keep and preserve in permanent form a full record of his proceedings, including a concise statement of each association examined, and, in his annual report, he shall report the general conduct and condition of the building and loan associations doing business in this State. Such report shall include the information contained in the statements required of the associations in tabulated form. (106 v. 510.)

Embezzlement by Officer of Building and Loan Association.

Sec. 12472. Whoever, being a president, director, trustee, member of a committee, secretary, treasurer,

attorney or other officer or agent of a building and loan association or savings association as provided by law, embezzles, abstracts or willfully misapplies any of the moneys, funds or credits thereof, or issues or puts into circulation a warrant or other order, or assigns, transfers, cancels or delivers a note, bond, draft, mortgage, judgment, decree or other written instument belonging thereto, or raises money otherwise, or receives money from a member or other person for and in the name of such association unless authorized so to do by the board of directors thereof, shall be imprisoned not less than one year nor more than ten years and be liable to the person injured thereby to the extent of the damage incurred. Suit may be brought against the person so violating and the sureties on his bond given to such association for the faithful performance of his duty. (99 v. 536-46.)

Signing Name to Order Without Authority.

Sec. 13188. Whoever, being a president, director, trustee, member of a committee, secretary, treasurer, attorney or other officer or agent of a building and loan association or savings association, as provided by law, signs the name of a person to an order or warrant for the payment of money without proper power of attorney or written order from the person to whose order such order or warrant is made payable, shall be imprisoned not less than one year nor more than ten years. (99 v. 536-46.)

Declaring Dividend Greater than Earned.

Sec. 13189. Whoever, being a member of a board of directors of a building and loan association or savings

association, as provided by law, votes to declare, or, being a financial or first secretary thereof, declares or advises the board of directors thereof to declare a greater dividend than has been actually earned by such association, for the purpose of deceiving the people or defrauding the members thereof, shall be imprisoned not less than one year nor more than ten years. (99 v. 536-46.)

False Entry in Book, etc.

Sec. 13190. Whoever, being a member of a board of directors of a building and loan association or savings association, as provided by law, certifies to, or makes a false entry on a book, report or statement of or to such association, with intent to deceive, injure or defraud it or another company, body politic or corporate or person, or to deceive any one appointed to examine the affairs of such association, shall be imprisoned not less than one year nor more than ten years. (99 v. 536-46.)

Aiding Officer to Violate Preceding Sections.

Sec. 13191. Whoever, with intent to deceive, injure or defraud a building and loan association or savings association, as provided by law, or other company, body politic or corporate or person, aids or abets a president, secretary, treasurer, committee or other person in violation of any of the next four preceding sections shall be imprisoned not less than one year nor more than ten years. (99 v. 536-46.)

Failing to Make Reports, etc.

Sec. 13192. Whoever, being an officer thereof, fails to make the reports required of him by the laws provided for the organization, regulation and inspection of building and loan associations or savings associations, or, being an officer, employee or other person,

solicits business for, aids or assists such association to do business contrary to the provisions of such laws, or without having complied therewith, shall be fined not more than five hundred dollars or imprisoned not more than six months, or both. (99 v. 536-46.)

Liability on Bond.

Sec. 13193. Whoever violates any provision of the next five preceding sections shall be liable to the person injured thereby to the extent of the damage incurred and suit may be brought against the person so violating and the sureties on the bond given by him to such association for the faithful performance of his duty. Fines collected under the next five preceding sections shall be paid into the State treasury. (99 v. 536-46.)

"TREASURY DEPARTMENT,

Office of

COMMISSIONER OF INTERNAL REVENUE

WASHINGTON, *Jan.* 30, 1918.

Mr. GEO. S. WALKER,
Building and Loan Commissioner,
604-606 Claus Spreckels Bldg.,
San Francisco, Calif.

SIR:

Receipt is acknowledged of your letter of the 18th instant, in which you ask to be advised whether or not Building and Loan Associations having a permanent guarantee capital and those loaning money to others than members of the Association are exempt under the provisions of the Act of September 8, 1916, and Titles I and II of the Act of October 3, 1917.

In this connection the following extracts from your letter are quoted:

First. Under the laws of this and one or two other States, Building and Loan Associations may have a permanent guarantee capital stock, which is nonwithdrawable, and in practice participates in common with installment shares, besides which it receives a bonus, in some cases equal to one (1) per cent of the average loans in force. The law provides that this stock shall be subject to all the conditions and liabilities attaching to the paid-in capital stock of other classes of corporations, and shall protect and guarantee all other stockholders and creditors against any loss.

Second. Under the laws of this and certain other States, Building and Loan Associations may—and in very many cases do—loan to others than shareholders or members; and especially is this the case where they have a permanent guarantee capital, and the working capital comes from other sources than installment and full paid-up shares.

In reply you are informed that Building and Loan Associations organized and operated in accordance with the laws of the State in which they are organized and do business are exempt from the provisions of the law referred to above. Therefore, if a Building and Loan Association in your State, which transacts business in accordance with the information contained in your letter, does so under the authority conferred upon it by the laws of the State of California, then that fact does not destroy its exemption under the provisions of the acts cited.

Respectfully,

DANIEL C. ROPER,
Commissioner."